

## **Tutorial 1: The Open Economy and Exchange Rates**

1. Which activities define an open economy? How can the openness of an economy be measured? Which economies are likely to be more open?
2. What are the implications of a deficit on the external current account for the balance between an economy's saving and investment? When would an external current account deficit be unsustainable?
3. Distinguish between the current and the capital account of the balance of payments. Why must the balance of payments always balance?
4. Distinguish between the nominal and the real exchange rate. Do these two exchange rates necessarily move together?
5. Which kind of exchange rate regimes can an economy opt for?
6. How can the equilibrium exchange rate be determined? When would an exchange rate level be unsustainable?
7. Does a devaluation of the (i) nominal exchange rate and (ii) real exchange rate necessarily lead to an improvement in the external current account?